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Greenhouse Gas Reduction Scheme Transition Review
NSW Department of Water and Energy
Level 17, 227 Elizabeth Street
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ggastransition@dwe.nsw.gov.au

Dear Sir/Madam

Forests NSW is an accredited provider under the Carbon Sequestration abatement category of the NSW Greenhouse Gas Reduction Scheme (NSW GGAS). In 2005 we undertook the world's first registered trade in forest based carbon sequestration and have since registered over 1.29 million certificates (NGACs) through the NSW scheme.

Forests NSW seeks to make comment on the following issues identified in the *Transitional arrangements for the NSW Greenhouse Gas Reduction Scheme Consultation Paper*:

1. The transition timeframe;
2. How forestry sequestration providers are to be treated;
3. What happens to unused NGACs;

1. The Transition Timeframe

Forests NSW registered approximately 23,000 hectares of eligible forest under the NSW GGAS prior to the Commonwealth Government making its commitment to a NETS. In doing so, Forests NSW agreed to the rules applying to carbon sequestration projects which included the registration of 'Restriction on Use' covenants over the Real Property Act land titles of its affected forest.

Under the NSW GGAS, 'Restrictions on Use' covenants apply for a period of 100 years and represent a significant encumbrance on affected land. Forests NSW agreed to these encumbrances after serious and careful consideration of the costs and associated benefits that would arise. In making this decision it was assumed that the full carbon sequestration benefits from our eligible forests could be realised. By 2010 about 60% of the carbon sequestration benefits arising from these forests, as determined by the NSW GGAS trading rules, will have been realised.

It is possible that the NETS may not recognise forest offsets and or the carbon sequestration rules that apply under the NSW GGAS. If either of these scenarios eventuates, Forests NSW would seek to be released from its obligations under the

NSW scheme and in particular the removal of the 'Restrictions on Use' covenants which apply to its NSW GGAS registered forest.

2. How forestry sequestration providers are to be treated

On 17 March 2008 the Commonwealth Government announced a timetable for the introduction of an emissions trading scheme with commencement scheduled for 2010.

Phase 1 (March to June 2008) of the timetable involves consultation with stakeholders to inform them of development of a Green Paper on scheme design. Phase 1 specifically includes consultation with the agricultural and forestry sectors on the question of their inclusion in the ETS and on the timeframe for that inclusion.

It is understood that the Commonwealth Government is considering three broad options on how forests may be treated:

- I. *Excluded* from the scheme – neither storage of carbon in new forests nor emissions through harvesting would be subject to a carbon cost, though other measures may apply in the sector. The forest sector would not be able to gain credits and would not be exposed to liabilities for emissions from harvesting (though the emissions associated with fuel use, fertiliser, etc would be covered).
- II. *Offsets* (not covered but participating as offset projects) – a project would need to demonstrate improvements compared to a baseline in order to generate credits, and may need to demonstrate permanence (carbon stocks for 70+ years) and additionality ("new" projects). Other forest impacts would not be covered.
- III. *Covered* – the storage of carbon in growing forests and emissions through harvesting would be the subject of a carbon cost.

Forests NSW believes that the treatment of forestry offset providers under the NSW GGAS will be influenced by how forests will be treated under the NETS. We do not necessarily share the NSW Department of Water and Energy view that "forestry offsets are likely to be a feature of the NETS", as any of the three options above are foreseeable outcomes of the NETS design. Forests NSW would hope that forests are either covered or treated as offsets in the NETS.

However, Forests NSW has some concerns about any intention to base the NETS offset scheme on the existing Greenhouse Friendly rules. Forests NSW support the commitment to review the Greenhouse Friendly Scheme prior to the development of longer term arrangements.

Forests NSW would welcome an opportunity for further comment on the NSW GGAS transitional arrangements once the Commonwealth Government's intentions on its preferred treatment of forests in a NETS are made known.

3. What happens to unused NGACs

Due to the nature of the rules of NSW GGAS, carbon sequestration abatement providers are highly exposed to the transitional arrangements for unused NGACs.

Forestry carbon sequestration abatement providers, in calculating the number of NGACs that arise each year from their NSW GGAS registered forests, can only quantify the number that arises. In simple terms the trees continue to grow and sequester carbon which if value is to be recognised the quantity must be registered.

Forestry carbon sequestration abatement providers cannot therefore 'manipulate' the production of carbon on an annual basis. Due to these restrictions it is inevitable that forestry carbon sequestration abatement providers will be left with NGACs at the commencement of a NETS.

Due to the scale of Forests NSW carbon sequestration business the number of NGACs it is likely to be left holding will be substantial. While for some time the market for NSW NGACs has been thin, due in part to uncertainty about the design framework of the NETS, any NSW Government policy signal that allows NGACs to be discounted against NETS permits may be expected to seriously undermine the current trading value of NGACs.

For the reason outlined, Forests NSW strongly recommends that the NSW Government adopt a firm stance in its negotiations with the Commonwealth and insist that unused NGACs be allowed to be converted to NETS permits on a tonne for tonne basis at the start of the NETS.

Thank you for the opportunity to comment on the transitional arrangements consultation paper. We are available to provide further input on this issue once the treatment of forests within the NETS is made known.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Nick Cameron', followed by a period.

Nick Cameron
Manager, Investor Relations
FORESTS NSW